



Draft
2008 RECESSION & TOW
Implications for Our TOW Scenarios

Background & Introduction

The current fiscal crisis and looming economic recession is on all our minds these days. It is understandable that there are questions regarding our transfer of wealth (TOW) scenarios given these challenging times. Intuition and daily experience strongly supports the view that reality has changed and so must our scenarios. In response to these questions we have prepared the following response.

Implications for Our TOW Scenarios

- We are in a new reality and it is clear that we are experiencing possibly the worst financial crisis since the Great Depression. It also appears very likely that we are entering into a potentially severe economic recession both nationally and globally. No one knows for sure the depth and duration of these challenging times - but wealth in America is changing as a result of these events.
- Our TOW scenario model is based on historic economic relationships and informed by emerging trends in demographics, economics and wealth formation by American households. Because our history is complete with economic recessions we have incorporated into our scenario model at least one recession for each decade over our 50 year projection horizon. We assume at least two of these recessions are severe. This assumption ensures our scenario is reasonably conservative.
- Additionally, our TOW projections are conservative in the sense that we assume the following:
 - Economic growth in the future will be slower when compared to the past.
 - The ability of households to convert income into new wealth will occur at lower rates in the future than in the past.
 - We exclude from our calculations certain assets such as motor vehicles, boats, art, jewelry and other like assets.
 - We discount wealth associated with family owned business, farm ground, recreational land and other closely or jointly held assets.

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- Current net worth for America's households peaked at nearly \$59 trillion in the third quarter of 2007. Since then it has dropped to just under \$56 trillion in the second quarter of 2008. [Source: U.S. Federal Reserve Bank, 9/18/08] There is a strong reason to believe that further erosion of household's current net worth will continue into 2009. Loss levels could rise to \$5 trillion before the trend line turns positive. **Because of the timing of this downturn, we believe our 10-year (2005 to 1015) TOW projections are overly optimistic and should be adjusted downward by 5%.**
- Because our model incorporates recessions over the entire 50 year period we do not believe our 50-year TOW projections need to be adjusted at this time. In any economic downturn asset loss is both temporary and permanent. Some wealth will be lost forever. However, certain assets such as stocks and homes may be depressed in value now, but will recover to higher levels once an economic recovery becomes more widely recognized. For example a stock valued at \$50 per share today may rebound to a significantly higher price say \$85 per share once market fundamentals overcome fear. What has happened in every recovery following every recession since 1929 is a wealth rebound that overcomes part of the wealth losses realized during the downturn.
- Beyond the personal crisis of a failed family business, job loss or mortgage foreclosure, the news of housing value losses and the recent 401K retirement fund losses are weighing heavy on most Americans today. Losses are real and for those with exposure to real estate and stock markets approaching retirement - the losses can be devastating. But overall perspective is important. Again looking at the most recent Federal Reserve household wealth data (as of the close of the 2nd Quarter of 2008) roughly 37% of all household assets were in tangible wealth like homes. The balance is in financial wealth such as retirement, savings and the stock market. Considering all household assets, about 14% of household wealth is exposed directly to stock market changes.
- Like all Americans we will continue to closely monitor developments and do our best to keep those of you who are using our TOW Analysis informed of the viability of our past scenarios given these changes. We do recognize some regional and state areas will be more directly impacted. Feel free to call us and we will do our best to help you measure how the current crisis might impact the scenarios we have completed for you.

Conclusion

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America has seen very hard times before. Fortunately, since the Great Depression our ability to manage our economy has greatly improved. For those who have not experienced a severe economic downturn before, the current crisis can feel like the world is on the edge of economic depression. While we do not know what 2009 and beyond might look like, we have great faith in the world's ability to manage this crisis and return us to more positive economic times. The lessons of history can provide perspective and insight. These lessons suggest that we will grow out of this crisis and in time better times will return - hopefully by the second half of 2009.

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On behalf of the RUPRI TOW Team

Questions and Additional Information

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